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Remarks

FYI--The attached paper was received from The
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Executive Secretary

18 June 86

Date

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THE WHITE HOUSE
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CABINET AFFAIRS STAFFING MEMORANDUM

Date: 6/2/86 Number: 317, 130 Due By: 31713025
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F6010-04Subject: Economic Policy Council Meeting - June 4 '86
IT008Roosevelt Room
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ALL CABINET MEMBERS

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Chew (For WH Staffing)

Executive Secretary for:

DPC

EPC

REMARKS:

The Economic Policy Council will meet on Wednesday, June 4, 1986 at 1:00 P.M. in the Roosevelt Room.

The agenda and background papers are attached for your information.

RETURN TO:

☒ Alfred H. Kingon
Cabinet Secretary
456-2823
(Ground Floor, West Wing)

☐ Don Clarey
☐ Rick Davis
☐ Ed Stucky

Associate Director
Office of Cabinet Affairs
456-2800 (Room 225, OEOB)

THE WHITE HOUSE
WASHINGTON

ECONOMIC POLICY COUNCIL

June 4, 1986

1:00 p.m.

Roosevelt Room

AGENDA

1. U.S.-EC Trade Strategy
2. GATT Objectives

ECONOMIC POLICY COUNCIL MEETING

June 4, 1986

PARTICIPANTS

Secretary Baker, Chairman Pro Tempore

Secretary Lyng

Secretary Baldrige

Secretary Brock

Secretary Herrington

Director Miller

Ambassador Yeutter

Deputy Secretary Whitehead

(Representing Secretary Shultz)

Deputy Secretary Darman

Thomas Moore, Member, CEA

(Representing Chairman Sprinkel)

John Svahn, Assistant to the President for Policy Development

Alfred H. Kingon, Assistant to the President and Cabinet

Secretary

Eugene J. McAllister, Executive Secretary

Additional Attendees:

William Ball, Assistant to the President for Legislative Affairs

Steve Danzansky, Special Assistant to the President for

International Economic Affairs, NSC

Boyden Gray, Counsel to the Vice President

W. Allen Wallis, Under Secretary of State for Economic Affairs

Arnold Burns, Associate Attorney General

[] Acting NIO for Economics, CIA

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THE WHITE HOUSE

WASHINGTON

June 2, 1986

MEMORANDUM FOR THE ECONOMIC POLICY COUNCIL

FROM: EUGENE J. McALLISTER *EM*
SUBJECT: Agenda and Papers for the June 4 Meeting

The agenda and papers for the June 4 meeting of the Economic Policy Council are attached. The meeting is scheduled for 1:00 p.m. in the Roosevelt Room.

The first agenda item will be a discussion of U.S.-EC trade relations and strategy. The TPRG has developed a paper outlining the major issues in U.S.-EC trade and offering several recommendations for actions to better manage U.S.-EC trade issues. The paper is attached.

The second agenda item will be a discussion of U.S. objectives in a new GATT round. The TPRG has reviewed our GATT objectives and identified a number of possible barriers to initiating a new round at the September Ministerial meeting. A paper prepared by the TPRG describing these barriers and assessing their significance is attached.

SECRET AND CONFIDENTIAL ATTACHMENTS

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THE UNITED STATES TRADE REPRESENTATIVE
WASHINGTON
20506

June 2, 1986

MEMORANDUM FOR THE ECONOMIC POLICY COUNCIL

FROM: TRADE POLICY REVIEW GROUP
SUBJECT: U.S.-EC Trade Strategy

I. Issue

The fundamentals of our trade relationship with the EC are changing dramatically in the decade of the 1980s. EC and U.S. perceptions of the relationship lag behind the realities. Despite the fact that the bulk of U.S.-EC trade takes place without controversy, the number and severity of U.S.-EC trade frictions are increasing. In order to manage these frictions and pursue U.S. interests successfully, we need to understand the underlying realities and to define clearly for ourselves and the EC our objectives.

II. Structural Problems

Structural problems underlie the increase in U.S.-EC trade frictions.

- o Formation of EC did initially contribute to European economic progress.
- o Oil shock of 1973, 1979-1980 traumatized European economy.
- o Effects linger on:
 - unemployment remains high;
 - slow growth a paralyzing phenomenon.
- o Community's energy has been absorbed in digesting first enlargement, which took place on eve of first oil shock, and in negotiating entry of Spain and Portugal. A larger and less cohesive Community will be even more difficult to deal with. On many issues, EC has switched emphasis to protection of what it has.

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- Europe's high average unemployment, now at 11 percent EC-wide, masks regional pockets even higher.
- Problems include overly generous unemployment and employee benefits packages, rigid hiring and firing practices, housing programs that hamper worker mobility, disincentives to employment-generating investment, and interference with business decisions on when and where to open or close plants.
- o By freezing labor and capital into inefficient activities, Europe has reduced its opportunities to grow and expand into more dynamic activities where it might compete better in international markets.
- o This is a matter of direct concern to U.S.
 - Economic weakness on part of strategic partners can diminish Atlantic alliance's capabilities.
 - From an economic perspective, rigid economies and anemic growth are mutually reinforcing and generate adverse effects on Europe's trading partners, e.g., Europe is not absorbing its "share" of LDC-manufactured exports.
- o This has created problems in both industry and agriculture.
- o The CAP has compounded European difficulties by sapping resources which might be used to promote productive investment; it is in the agricultural sector where our major trade problem lies.
- o The EC's industrial trade and investment regime is generally open, with relatively few commercial problems. The large stock of foreign direct investment has smoothed relations in manufactured goods. There are, however, continuing internal pressures in the EC to use subsidies and protectionism in key sectors--now basically steel, telecommunications, Airbus, and heavy electrical equipment. The major industrial concern is that these pressures may grow significantly under conditions of continued slow EC economic growth and structural problems.

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- o The ability of the EC Commission to deal with these problems--and with us--is limited by its institutional weaknesses: In many areas it has no authority (services, tax, and fiscal policy); in others it must obtain approval of the 12 diverse Member States.
- o Whether and how Europe addresses its economic problems has major implications for trade and investment relations. Moreover, the failure of Europe to grow adequately could weaken U.S.-European political and security relations.

III. U.S. Objectives

A. General

- Increase U.S.-EC trade with less friction.
- Encourage meaningful EC structural adjustment, particularly in agriculture.
- Increase economic flexibility in Europe by encouraging EC to have a more open, more private sector-based economy.
 - Reduced rigidities will encourage economic growth and reduce the need to subsidize.
- Broaden U.S.-EC trade dialogue to include more critical issues in addition to agriculture, such as telecommunications, services, aerospace, and heavy electrical equipment.

B. Agriculture

- Increase market access into EC.
- Reduce effects of the CAP on world agricultural trade.
 - Continue efforts to persuade EC to eliminate export subsidies.
- U.S. and EC agree on reforms necessary in agricultural regimes globally to minimize future conflicts.

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C. Industry/High Tech

- Encourage the EC to continue to keep its industrial trade and investment regimes generally open.
- Discourage the operation of businesses on a non-commercial basis. Encourage privatization. Discourage EC tendency to promote regional "flagship" companies when not commercially sensible.
- Encourage Europe to continue to build commercially viable advanced technology capabilities through non-subsidized, market-oriented policies. Discourage Europe's efforts to produce redundant high technology capabilities through subsidies and protection.
- Enforce multilateral and U.S. technology transfer policies and regulations in a manner that will prevent the transfer to Warsaw Pact nations of technologies critical to military use, but in a way that will promote and strengthen the high technology capabilities and economies of Europe.
- Increase market access into the EC.
- Major priority is to increase access into EC for telecommunications equipment and services, and heavy electrical equipment.
- Discourage EC Member State Governments and the EC Commission from intervening into U.S.-EC company competition in third country markets, e.g., Airbus.

D. Procedural

- Intensify contacts with individual Member States on economic/trade issues.
- Do not rely on contacts with EC Commission alone to achieve our objectives.

IV. Macroeconomic and Structural Approach

In its economic policy discussions with the EC, the U.S. has consistently advocated the pursuit of policies based on free market principles which will increase the sustainable, low-inflation growth potential of EC Members. Macroeconomic talks have covered the need to:

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- Reduce government budget deficits and overall involvement in the economy (e.g., government expenditures as a share of GNP);
- Pursue steady, predictable monetary policies to reduce inflation and expectations about future inflation; and
- Remove price controls.

On the structural side, we have discussed with EC Members the need to:

- Eliminate or reduce significantly regulation of financial and goods markets which hinder efficient resource allocation;
- Remove exchange rate and international capital controls and regulations;
- Remove restrictions on employment and disincentives to work in order to increase labor market flexibility; and
- Eliminate subsidies to inefficient industries.

Our purpose has been to increase the job-creating strength of Europe and to allow markets to function more efficiently.

In broad terms, recent OECD and Summit Communiqués have reflected these efforts. Widespread recognition now exists in Europe of the problems caused by excessive regulation of markets and, in turn, the effects of inflexibility on growth and job creation.

V. Agriculture

Agriculture is the sector in which the EC has achieved the highest degree of economic integration. It is also the source of most of our contentious disputes with the EC.

- o The Common Agriculture Policy (CAP) has successfully fulfilled two objectives:
 - It has allowed more people to remain in farming than would otherwise have been possible; and
 - It has increased EC self-sufficiency in agriculture.

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- o The CAP has failed in other respects:
 - Its high import barriers have reduced access to the EC market;
 - Its high guaranteed prices have resulted in production of surpluses which are not price-competitive in world markets; and
 - Its export subsidies have disposed of these surpluses, resulting in numerous trade disputes between the U.S. and the EC.
- o The EC has transferred some costs of the CAP to more competitive agricultural producers, including some third world countries, e.g., sugar producers.
 - Our recent agricultural disputes with the EC are a function of either EC subsidies or resulting surpluses.
- o Fulfillment of CAP objectives has been costly:
 - The high cost of the CAP (direct budgetary cost estimated at over \$18 billion dollars, indirect costs at \$60-\$70 billion annually) attracted serious EC attention a few years ago.
 - The VAT was increased and consideration was given to CAP reform.
 - Unfortunately, the high dollar and the 1981 Farm Act's unrealistically high loan rates took pressure off.
 - Despite expense of CAP and distortions and inefficiencies it promotes (both within Community and in terms of global trade), most EC Members not ready to abandon it.
 - The CAP has once again started to become uncomfortably expensive for the EC, with costs projected to increase by \$3 billion, or some 10 percent in 1986.
 - The EC this year faces a budget shortfall of \$2.9 billion due to larger export refunds on agricultural commodities.
 - Our lower loan rates now, which will induce more realistic world prices, will keep the cost of the CAP high and growing.

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- The Farm Act started this process; we need to make certain that any U.S. measures, legislative or otherwise, maintain this trend.

VI. Industry/High Tech

- o In contrast to agriculture, there have been relatively few industrial trade disputes with the EC.
 - Our primary dispute in this sector has been over steel, which is now covered by agreements. While semifinished steel remains a problem, we believe our chances are good of reaching an agreement in the next two to three months.
 - The fact of few disputes is due to EC receptiveness to the presence of a substantial U.S. multinational presence, and the openness of investment in the EC. The EC also has not maintained its competitiveness with the U.S. and Japan in many high tech sectors. This contrasts sharply with U.S. and EC disputes with Japan, which are heavily concerned with manufactures and high technology.
- o The EC is seeking to overcome its difficulties through a number of cooperative programs such as RACE, ESPRIT, and EUREKA. To date these programs have yielded little of value. Knowledgeable Europeans remain skeptical that these programs will be of much help.
- o A Europe which is increasingly uncompetitive is a Europe which will not be able to move toward a more liberal trading regime, perhaps resorting to protectionist actions, and finding it increasingly difficult to make the necessary adjustments out of declining industries.
- o Two areas of European advanced technology competition should be of particular concern to the United States: telecommunications and commercial aerospace. These two sectors, in particular, are presently the focal point of the EC's attempts to develop and sustain competitiveness in advanced technology manufactures. The U.S. should make every effort to make sure that the EC is aware that technology programs such as Airbus and the growing efforts to rationalize telecommunications capabilities must be commercially based.

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VII. Tactical Considerations

Constraints on the European Community

- o The Commission has a legal mandate to conduct trade negotiations, but must have Member State approval for any agreement. Because the Treaty of Rome requires a majority vote on trade issues, the Commission must achieve a consensus to resolve major issues.
- o Preservation of the CAP is often a major consideration behind EC trade policy. Despite the Commission's attempts to reduce spending on CAP programs, most of the Member States, with an eye to domestic farm voters, are reluctant to support any curtailment of CAP benefits.
- o The Commission tends toward inaction, since any proposal is subject to criticism by the Member States. The Commission tends to act only when a crisis arises and Member States demand action.
- o Those in the Commission responsible for U.S. relations in recent years have adopted a more hardline, less-pragmatic approach.
- o Expansion of the EC-10 to the EC-12 this year increases the complexity of decisionmaking in the EC..

Constraints on the United States

- o Europeans believe that European unity and economic integration are of such value to the U.S. for political and national security reasons that we should be willing to subordinate our economic/trade interests.
- o Rising global and bilateral trade deficits have left the U.S. with less room to maneuver, for either political or economic reasons, on bilateral trade issues.
- o Depressed agricultural prices in the U.S. have created increased pressures to maintain access to foreign markets.

VIII. Recommendations

Securing the objectives noted above--and thus strengthening the U.S.-EC relationship over time--will not be an easy task given the constraints on both sides. Thus, the EPC must consider a number of short- and longer-term tactics aimed at improving our trade relationship with the Europeans.

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Agriculture

- o Over the longer term we need (1) to develop a strategy to bring the EC--as well as our other trading partners--to the table to implement reforms in our agricultural regimes to avoid future conflicts, and (2) to reduce the effects of the CAP on world agricultural trade.
 - Recent discussions at the Summit and at the OECD Ministerial have shown a marked willingness on the part of our major developed country trading partners to begin discussions of the agricultural issue.
 - Negotiations on agriculture in the GATT in the New Round will provide the principal vehicle for generating a multilateral solution to the agricultural problem. Work in the OECD should support our efforts in the GATT. An EPC Working Group has been formed to examine our agricultural strategy in light of the Summit mandate.
 - In addition, the EPC directs that we step up bilateral approaches to the EC on long-term agricultural issues. The following should be included in that approach:
 - Ambassador Yeutter and Secretary Lyng will follow up on the bilateral dialogue begun in April.
 - Other fora for engaging the EC in bilateral agriculture discussions should be utilized.
 - We should actively enlist other countries as "allies" in opening a dialogue with the EC.
 - We should continue policies to increase the budgetary cost to the EC of the CAP.
- o Our short-term priority must be to resolve the Enlargement dispute.
 - With respect to the Portuguese measures, the EPC directs that we continue our strategy to seek termination of these GATT-illegal quotas. We should continue to press the EC to submit these measures to GATT dispute settlement procedures. If the EC will not agree to do so jointly, then the U.S. should do so unilaterally. If the EC counter-retaliates, we must be prepared to respond again.

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- With respect to Spain, we should ensure compensation for lost trade. If the EC refuses to provide compensation, we should, pursuant to the President's decision, initiate the process on July 1 which will result in our raising tariffs in August.
- We should press forward on the citrus and pasta negotiations as quickly as the enlargement environment allows. If the EC appears to lose its commitment to a timely resolution of these issues, the EPC will be asked to consider an appropriate response.

Industry/High Tech

- o The U.S. strategy must be aimed at eliminating the significant market barriers now existing in the industrial sector, and at preventing the spread of protectionism and European preference.
 - We should encourage policies and regulations that will promote and strengthen the EC's economic growth and structure.
 - We should use all opportunities to discourage the operation of commercial entities on a non-commercial basis, and to encourage entrepreneurship and privatization.
 - The U.S.-EC steel arrangement has minimized frictions, and will likely continue to do so until it expires in 1989. The EPC directs that a Steel Working Group begin exploring steps the U.S. and the EC could take to restore steel trade to a market orientation, including the elimination of subsidies so that trade restraints would not be renewed.
 - A key objective in the near term is to ensure improved market access in telecommunications. The TPRG is examining this issue and will have specific recommendations for the EPC shortly.
 - In the area of government support to high tech industries, the most visible near-term problem is Airbus. An initial meeting with the three Airbus countries in March will be followed by a second meeting in June. If we do not reach sufficient agreement, a plan will be prepared to raise this to a political-level initiative.

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- The EPC directs the TPRG to identify other sectors where we should begin a dialogue with the EC on the issue of government support.
- Efforts should be increased to ensure that programs such as RACE, BRITE, ESPRIT, and other EC and national technological programs allow the full participation of U.S. subsidiaries in Europe; and we should immediately seek the elimination of any European steps which reduce U.S. national treatment in Europe.
- We should seek to increase bilateral discussions with the Europeans that are COCOM members, to allay fears that U.S. technology transfer controls or extraterritoriality pose a threat to their technological utilization. We should act to defuse the growing perception of the U.S. as an unreliable supplier, so this cannot be used as an excuse to cover programs really taken for protectionist purposes--such as decreasing the use of U.S. components in the Airbus.
- We should examine the new EC-12 tariff schedule carefully to determine that it does not disadvantage U.S. companies unfairly, and we should seek compensation in strict accord with Article XXIV:6.

Macroeconomic/Structural

- o To increase the sustainable, low-inflation growth potential of EC Members, the United States should continue to use appropriate opportunities (G-5, G-7, OECD, Summits, and IMF) to urge policies to remove structural rigidities and improve macroeconomic policy management in the EC.
- The ongoing OECD structural adjustment study, scheduled for completion by the 1987 Ministerial, will support this effort. The EPC directs U.S. representatives to relevant OECD meetings to take steps in the coming months to ensure that (1) that report is shaped in a way that supports this policy goal; and (2) it receives sufficient attention both within and outside the OECD to assist European adjustment efforts.

Institutional

- o The annual December meeting of U.S. Cabinet officials and their EC counterparts provides one formal vehicle to review the full range of U.S.-EC economic relations. The EPC directs the TPRG to examine our contacts with the EC Commission and the Member States, and to make recommendations for improvements as appropriate.

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The Changing Fundamentals

- A. The EC as a whole is our largest trading partner.
- Total two-way trade of \$113 billion in 1985 accounted for about one-fifth of total U.S. trade.
 - Total two-way sales of U.S.-EC subsidiaries producing in each other's markets exceeds \$700 billion--making this the largest economic relationship in the world.
 - These numbers have grown with the expansion of the EC from 10 to 12 Member States on January 1, 1986.
 - The EC-12 has a population 34 percent larger and a GNP 35 percent smaller than the U.S.

Thus, we are dealing with an economic entity similar in size to the U.S.

- B. The EC is the world's largest trading entity.
- Internal trade among the EC-10 in 1984 comprised almost 15 percent of total world trade.
 - Total trade of the EC-12 constituted 31 percent of world trade in 1984.

C. The most significant development has been the recent large swing from surplus to deficit in our trade balance with the EC.

- From the formation in 1957 through 1982, the U.S. enjoyed a surplus in its trade account with the EC, with the exception of one year, 1972.
- In 1983, we had a deficit of \$2.3 billion, which grew dramatically each year, reaching \$23 billion in 1985. In large measure, the increase in the deficit has been due to the strength of the dollar.
- The trade deficit with the EC is projected to peak at about \$25 billion and then to fall significantly. The bilateral trade balance since 1972 has demonstrated a high degree of sensitivity to changes in the value of the dollar and GNP growth differentials.

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THE UNITED STATES TRADE REPRESENTATIVE
WASHINGTON
20506

June 2, 1986

MEMORANDUM

TO: THE ECONOMIC POLICY COUNCIL
FROM: THE TRADE POLICY REVIEW GROUP
SUBJECT: U.S. Objectives and Strategic Considerations for the
New Round of Multilateral Trade Negotiations

Issue

The GATT Preparatory Committee (PrepCom) for the New Round has reached a critical stage in its work. It has reviewed the thirty-odd issues proposed for inclusion in the new trade talks and is now drafting the declaration that Ministers will approve in September at a meeting in Uruguay to launch the new round.

The purpose of this paper is to:

- update the EPC on the PrepCom's work;
- reaffirm the U.S. objectives for the negotiations;
- clarify key current strategic and tactical considerations; and
- outline next steps.

The appendix describes key issues of interest to the U.S. and specific negotiating objectives we want to achieve for each issue. Additional issues proposed by other countries may also be acceptable to the U.S., but do not warrant EPC consideration at this point.

It is anticipated that the EPC will review our new round strategy and tactics, once the PrepCom has completed its work in mid-July and prepared a draft ministerial declaration. If necessary, the EPC could discuss the issue again just prior to the Ministerial meeting in September.

Background

-- Since the decision of the GATT Contracting Parties in November, the Preparatory Committee has met six times and set

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out an intensive schedule of meetings through mid-July. At that time, the Committee is to make recommendations, in the form of a ministerial declaration, on the objectives, subject matter and organizational details for the new round, as well as participation in it. The recommendations will be forwarded for action to Ministers, who will meet in Punta del Este, Uruguay during the week of September 15. We expect the Ministers will adopt the declaration and formally open the new trade talks.

U.S. Objectives for the New Round

-- We have four basic objectives for the new round. They are to:

- o seek trade liberalization as a means to increase global economic growth and to create expanded export opportunities for competitive American producers;

- o resist new protectionist measures and eliminate those now in place around the world;

- o strengthen and expand the rules of the trading system, including those that are currently deficient (such as agriculture and safeguards) and to develop new rules to deal with the increasingly important areas of international trade (such as intellectual property, investment and services); and

- o strengthen the GATT as an institution to make it relevant to the problems of today's trading environment and capable of dealing with those of the future as they arise.

-- These objectives are necessarily interrelated and, to be successful, we have to achieve all four.

Strategic Considerations

There are a number of strategic questions which must be resolved before the September ministerial meeting.

1. What are our priorities for the new round?

-- We face an uphill battle to get agreement -- not to mention agreement in September -- on the early launching of the new round which will be based on the agenda we have advocated. Nonetheless, the agenda for the negotiations must be both ambitious and comprehensive if we are to achieve meaningful agreements and lasting results. We must insist on the inclusion of key issues of principal importance to the U.S. (See appendix.)

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-- Does the EPC agree that establishing a rank ordering of issues for inclusion on the negotiating agenda is one trap we should avoid?

o Setting priorities would, by definition, single out certain items for priority treatment in the negotiations. Given the state of the trading system today, progress on all issues is critical.

o The identification of priorities could limit the agenda, and thereby jeopardize inclusion of items of importance to us. A negotiating agenda that failed to include agriculture or services, for example, would be clearly inadequate.

o The negotiating agenda also must reflect the interests of all countries. It will be difficult to encourage broad participation in the negotiations if the agenda is not balanced and the talks do not proceed on all subjects simultaneously. (It should be noted that balancing the agenda may require mentioning items that are not critical to us, such as restrictive business practices.)

o The rank ordering of issues at this stage also might limit our flexibility to introduce additional subjects, as appropriate, during the course of the negotiations.

-- From the domestic point of view, continuing private sector support is conditioned on the inclusion of issues of interest to particular industries or groups. It is, therefore, critical at the outset of the negotiations to ensure, to the greatest extent possible, that the agenda encompasses all issues of interest to our domestic constituents.

-- Although we want a comprehensive agenda and negotiations that proceed on all subjects simultaneously, we want to have meaningful results as soon as possible. It may be feasible to conclude agreements or interim understandings on certain issues in advance of others. This may be particularly true with issues that have long been the subject of debate and negotiation in the GATT, such as agriculture and safeguards. However, our desire to reach early agreement should not be misinterpreted as an implied higher priority for these issues.

2. What is our position on standstill/rollback?

-- To set a positive tone for the start of the negotiations and lend credibility to the process, a number of developed and developing countries support a political-level commitment by

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trade ministers to a "standstill and rollback" of protectionist measures. Proposals being circulated in Geneva call for trade ministers to commit their governments at the start of the negotiations (presumably at the Ministerial meeting in September) not to introduce new protectionist measures, and to progressively dismantle existing trade restrictions during the course of the negotiations.

-- There are two issues at hand: one is the precise definition of the terms "standstill" and "rollback"; the other is the nature of the commitment. To be acceptable to the U.S., the coverage of the standstill/rollback commitment should:

- o leave us free to enforce antidumping, countervailing duty, Section 201 and other existing trade law provisions without any change;
- o enable us to use Section 301 to address significant unfair foreign trade practices, so long as the cases are pursued in a GATT-consistent way. (FYI. This may require very careful selection of targets and, in some cases, the following of additional dispute settlement steps in the GATT. To retaliate against unfair foreign trade practices without GATT authorization, such as we did recently against the EC on citrus and enlargement, would be inconsistent with such a commitment. END FYI);
- o be undertaken by all other GATT members, whether developed or developing; and
- o closely link agreement to the "standstill" with a credible program to "roll back" existing trade restrictions that are not maintained under the GATT system or under GATT auspices. (This would exclude measures that are consistent with the Multifiber Arrangement, but would not exclude our voluntary restraint agreements.)

-- As for the nature of the commitment, it is essentially a political -- not a legal -- one. Countries would obtain no additional GATT rights by accepting the commitment. In the event we violated the commitment (for example, by extension of the manufacturing clause), we would face retaliation by affected countries, just as we would without a standstill/rollback commitment. However, if we violated the commitment in a massive or repeated way, the negotiations would almost certainly come to a halt, given the importance that numerous GATT countries attach to a meaningful standstill and rollback pledge.

-- Is the EPC prepared to accept a standstill/rollback commitment, provided our trading partners did the same, that would restrict our ability to:

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- o put into place new voluntary restraint agreements except in those instances where there is a GATT cover; and
- o retaliate against unfair foreign trade practices under Section 301 except as authorized by the GATT?

3. What should our position be on providing favored treatment for LDCs in the new round?

-- Developing countries have pressed for inclusion in the ministerial declaration of a commitment by developed countries to grant LDCs special and more favorable treatment in every phase of the negotiations. We believe this is an unnecessary objective for the negotiations.

-- We recognize the principles for special treatment contained in Part IV of the GATT and do not intend to rewrite them; rather, our concern is with their appropriate application. In order for any reference to special treatment for LDCs to be acceptable to us, we have to reach agreement to close the giant loopholes that prevent the advanced developing countries from any meaningful discipline over their trade practices and "graduate" these countries from special status.

-- We anticipate that this issue will be a major bone of contention over the next few months. We are likely to come under increasing pressure from a number of our developed country trading partners to cave early on this point. Is the EPC agreed that a critical new round objective for us is to substantially reduce the level of special GATT treatment that the most advanced and internationally competitive developing countries receive?

4. How should we deal with trade-offs among issues?

-- This round will focus on developing more effective and enforceable rules with respect to government policies and practices affecting trade. As far as practicable, we seek self-contained agreements, where the "concessions" countries make are acceptance of new, higher standards of disciplines over their trade-distorting practices.

-- An essential element of the negotiations will be to strengthen the GATT as an institution. This includes not only measures to improve its internal operations, such as dispute settlement, but also steps to enhance the GATT's stature in the international community vis-a-vis the IMF and World Bank. Such institutional reforms would bolster the credibility of the GATT, and are, therefore, in each country's self-interest.

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-- There will be far less emphasis on the traditional exchanging of tariff concessions than in previous rounds, primarily because tariff levels are generally low and pose less significant trade distortions. However, we do have some important market access objectives that will require the reduction of foreign tariffs, as well as some of our own.

-- From a domestic point of view, we envision many difficulties with the inevitable trade-offs that will arise in the course of the negotiations. Is the EPC agreed that, to the greatest extent possible, our negotiators should seek to minimize trade-offs between different areas of the negotiations?

Tactical Considerations

To ensure the successful conclusion of the PrepCom's work between now and mid-July and a successful launch of the new round in September, we must focus on a number of tactical issues.

1. How do we counter those who argue for two Ministerial meetings?

-- We have reports that certain countries, including some in the EC and Brazil, have quietly suggested in Geneva that "conditions may not be right" for the ministers to launch the new round in September, and that a second Ministerial meeting (presumably next year) would be required. This is purely a stalling tactic, which we need to counter.

-- The CP's decision last November clearly states that the ministers, acting on the PrepCom's recommendations, will adopt a program for the negotiations in September. The President has personally pressed for an early start for the negotiations at the past three Economic Summits.

-- Is the EPC agreed that, the U.S. should reject proposals for two ministerial meetings to launch the new round? If so, EPC members should use all international economic and political contacts to press our arguments for a single, decisive meeting in September. USTR will coordinate a program of high-level demarches to make clear that if ministers fail to launch new negotiations at that time, the U.S. will pursue unilateral, bilateral or plurilateral measures to resolve trade problems.

2. How do we address the "Japan problem" in the new round?

-- The Japanese have been very supportive of the new round and have actively participated in the multilateral preparatory process. They are particularly vocal on the need for negotiations on trade in services and intellectual property.

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-- Nonetheless, access to the Japanese market is vitally important to the U.S. It is an equal concern of many other GATT members, some of whom have not attempted to penetrate the Japanese market but see future opportunities there.

- o Japan's restrictions on agricultural imports are among the most stringent in the world;

- o Japan imports a disproportionate share of total LDC manufactured exports (7% versus 64% by the U.S. and 24% by the EC); and

- o as a share of GNP, Japan's level of manufactured imports is not only the lowest for all industrial countries, but is declining. Their share dropped from 2.29% in 1980 to 2.16% in 1985.

-- Many of our trading partners would like to join us in using the new round to make the multilateral case for meaningful market-opening actions by Japan. The EC spokesman in Geneva has put down a marker that the Community will not negotiate without assurances that Japan will make market-opening concessions in the new round. That theme has been reiterated by various member states, as well as other GATT Contracting Parties in bilaterals and other fora.

-- Is the EPC agreed that we also expect a significant improvement in access to the Japanese market as a result of the new round? If so, how should we pursue this issue?

3. What should be our position on textiles in the PrepCom and the new round?

-- Last February, the President approved a strategy for renegotiating the multifiber arrangement on a fast-track to ensure that a renewed MFA is in place prior to the start of the new round. Negotiations in Geneva are proceeding more slowly than anticipated, however. As a worst case, we may face the prospect of entering the Ministerial without a renewed MFA. At the same time in the PrepCom setting, numerous LDCs have pressed for concessions on textiles -- or at least agreement to negotiate textile trade liberalization -- as a prerequisite to the new round.

-- Given our position on the need for an ambitious and comprehensive agenda for the new round, it is difficult for us to argue that textiles should be excluded from the negotiating agenda. The question comes down to largely one of timing.

-- The EPC should be aware that there is some discussion in Geneva that the price for launching the new round in September

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may be agreement to include textiles in the talks. Obviously, this is a decision that should not be made until the last possible moment in September -- well after we deal with the veto override effort on the textiles bill and after we have a clearer picture of Hill action on trade legislation.

-- Is the EPC agreed that, if textiles must be included on the new round agenda, we should seek to avoid any prejudice to the substantive treatment of the issue pending renewal of the MFA?

4. How do we press our substantive case most effectively between now and September?

-- As noted above and outlined in the Appendix, we have proposed an ambitious agenda for the new round. We have mounted campaigns to educate our trading partners on some "new" issues of critical importance to us -- investment and intellectual property. These issues were pursued through various demarches in capitals, Washington and Geneva.

-- What additional steps should we take between now and September to:

- o clarify our position on the various items on the U.S. negotiating agenda;
- o continue to "sell" our ideas internationally; and
- o convince the Congress to support an aggressive and ambitious new round agenda?

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APPENDIX

Specific Negotiating Issues of Interest to the U.S.1. Agriculture

-- Developing meaningful discipline over trade in agriculture is an imperative objective for the U.S. and the vast majority of GATT members. The EC, as was the case in the Tokyo Round, is doing its best to restrict the nature of negotiations on agriculture and to slow all progress. Nonetheless, the Community is the source of many of our problems with agricultural trade and we should not be dissuaded by their foot-dragging.

-- We seek to bring agriculture under effective trading rules and disciplines by eliminating import restrictions on agricultural products, treating agricultural export subsidies no differently than subsidies for industrial products, and eliminating other barriers to market access in both developed and developing countries.

-- We should not address agricultural problems exclusively in an agricultural group. Rather, we seek to address problems in agricultural trade in all relevant areas of the negotiations -- be it in a group dealing with subsidies, or market access -- so that no participant will be able to block progress on this issue of vital importance to U.S. export interests.

2. Safeguards and Other Temporary Import Measures

-- For a large number of GATT members, including the U.S., it is essential to reach a comprehensive agreement over the use of safeguard actions, that is emergency actions taken by governments to protect domestic industries from an influx of imports, thereby giving them time to adjust to competition. Most current safeguard practices have little to do with the disciplines of the GATT.

-- We seek to develop a comprehensive agreement disciplining the use of all safeguard actions, including voluntary restraint agreements and orderly marketing arrangements. Such actions should be temporary, transparent, degressive, and contribute to -- not retard-- adjustment, without shifting the burden of that adjustment on to other trading countries.

-- Comparable rules also must be developed to discipline all temporary measures taken by developing countries to restrain

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imports, such as the exemptions available to developing countries under the GATT rules for infant industry and balance-of-payments measures. This is an area where GATT rules are particularly lax.

3. Review of GATT Articles and Tokyo Round Agreements

-- Not surprisingly, the first effort to negotiate meaningful international disciplines over non-tariff barriers during the Tokyo Round was not perfectly satisfactory. What we need to do now is build on our experience with the codes over the past six years, expand participation, update certain provisions, and strengthen and improve their operation. We want to give particular attention to the standards, government procurement, aircraft and subsidies codes.

-- Negotiations on improvements to the codes do not necessarily have to be part of the new round, but rather could continue on their present track and be implemented before the new round is completed. At the same time, the broad negotiations might provide leverage for completing certain aspects of the code improvements, for example expanding entity coverage for the Government Procurement Code.

-- The U.S. should support a review of GATT articles as part of the negotiations. We would welcome improvements in certain provisions, such as Article XVII which stipulates that government trading entities should act in accordance with commercial considerations and GATT principles of non-discrimination. Such reviews should be undertaken with the aim of making these rules operational and enforceable.

4. Intellectual Property Protection

-- A key issue of interest to many in the private sector is negotiation of a code on intellectual property similar to the codes negotiated in the Tokyo Round.

-- We have proposed that our trading partners join us in developing such a GATT code, which would supplement existing international conventions, and ensure that measures taken to protect intellectual property do not distort international trade flows. We envision the code will have several elements, including binding provisions on transparency of regulations, notification, and dispute settlement.

-- One element of the negotiation of intellectual property should be to complete the work begun during the last round on a code to deter the importation of counterfeit trademarked merchandise.

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5. Investment Issues

-- Existing GATT disciplines cover trade but not investment distortions. Yet, the effect of government investment policies can be as distorting as any other non-tariff barrier. We, therefore, seek agreement on specific disciplines over government investment policies and measures.

-- A maximal approach would call for inclusion of the broad investment issue on the new round agenda, with a view toward developing an agreement or separate code with binding provisions governing national treatment, right of establishment, transparency of regulations, notification, and dispute settlement.

-- A number of countries have suggested that the U.S. is being too ambitious by suggesting that all investment measures be brought under GATT discipline. Some have argued that we should limit our proposal to trade-related investment measures only, such as trade distorting export performance requirements and local content requirements.

-- We are continuing an intensive effort to build support for the inclusion of the broad investment issue in the new round, but given the opposition to date, this is an issue that may not be resolved until the ministerial meeting in September.

6. Trade in Services

-- The U.S. has strongly advocated the development of international disciplines over the fastest growing segment of our domestic economy and export trade, that of trade in services. Our major trading partners joined us in calling for the inclusion of services in the new round at both the OECD Ministerial and the Tokyo Economic Summit. In addition, a number of developing countries have expressed a willingness to include services as part of the new round. However, a core group of developing countries, led by Brazil and India, are acting as though they are determined that services will not be included in the negotiations.

-- We want to use the new round to establish, under the auspices of the GATT, a framework of principles and procedures, that will provide for the maximum opportunity for international transactions in services trade. These include national treatment, transparency of regulations, notification, role of monopolies, and dispute settlement.

-- Consensus on the broad principles should enable us to identify concrete applications through the development of sector-specific understandings. Work currently underway on the services portion of the U.S.-Israeli Free Trade Agreement may serve as a

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useful model for the multilateral exercise.

7. Trade in High Technology Products

-- High technology is an increasingly vital component of American production. While we have come to recognize that separate negotiations on a "high technology code" is an unworkable solution to the trade challenges facing high technology industries, we have changed only our approach, not our objectives.

-- High technology considerations, and the industrial targetting strategies they often encourage, will be a critical part of the negotiations, in particular, in such areas as government procurement, standards, subsidies, intellectual property protection, and tariffs.

8. Worker Rights

-- Just as high technology considerations are important to many areas of the negotiations, so too are worker rights. We should ensure that trade expansion is not an end in itself, but that it benefits all workers in all countries.

-- In opposing an amendment to make denial of "internationally recognized worker rights" an "unreasonable" practice in Section 301 cases, the Administration has stated that worker rights questions are better pursued in the new round. Unless we make a credible effort in the GATT, it will be difficult to forestall legislative initiatives on the Hill.

-- We have told our trading partners that worker rights should be considered in the new round in some form. While we have not yet proposed any particular negotiating approach, an appropriate start would be to examine worker rights in light of GATT articles and the overall objectives of the GATT. So far, no other country has supported our effort, as they believe worker rights is beyond the scope of the GATT.

9. Market Access

-- An essential part of the negotiations is to substantially reduce barriers, both tariff and non-tariff, to our access to foreign markets. Competitive American firms need better access to foreign markets in order to take advantage of the lower value of the dollar and increase export sales.

-- Our private sector advisors have already begun to identify a number of areas where foreign tariffs remain a significant barrier to trade -- in such diverse areas as carpeting, ferrous and non-ferrous metals, furniture, chemicals, paper, telecommunications, and agriculture. We will similarly have to

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reduce some of our own tariffs.

-- Another area where tariff negotiations are necessary is to get commitments from developing countries to "bind" their tariffs under GATT rules so that they are not free to increase them without justification.

-- With regard to non-tariff barriers, we seek total elimination of GATT illegal quantitative restrictions, without concessions by other trading partners. We also seek the progressive phase-out of quantitative restrictions maintained under GATT rules. This includes the U.S. Section 22 waiver on agricultural products and the MFA. In addition, we seek to reduce the trade-distorting effects of other non-tariff barriers.

10. Strengthening the GATT as an Institution

-- An important area of the negotiations will be to develop ways to improve the functioning of the GATT system and to strengthen the GATT as an institution that is viable, credible and responsive to the changing conditions of international trade and the trading community.

-- Specifically, we seek:

o some specific improvements in the procedures of the dispute settlement process to ensure that countries have every opportunity to resolve their differences effectively and in a timely manner. It makes little sense to improve the trading rules without also improving the enforcement mechanism.

o other improvements in the functioning of the system, including greater ministerial involvement, improved and strengthened notification and surveillance requirements, and an enhanced "steering" mechanism to guide GATT operations.